

**Town of North Andover**  
***Financial Reserve Policies***

*Adopted by the North Andover Board of Selectmen on February 10, 2014*

*Adopted by the North Andover Finance Committee on February 5, 2014*

*Updated and adopted by both the Board of Selectmen in April 2015 and the Finance Committee in May 2015*

Fund balance and reserve policies should be established to protect the Town from unforeseen increases in expenditures, reduction in revenues, or a combination of both, or any other extraordinary events. Fund balance and reserve policies also serve to provide an additional source of funding for capital construction and replacement projects. Reserves should normally average 5% to 15% of the Town's General Fund budget.

There are two classes of reserves: 1) restricted reserves which are to be utilized only for the purpose designated, 2) unrestricted reserves which can be utilized at the discretion of the authorized personnel.

Reserve policies cover; Operating Reserves, which provide for unanticipated expenditures or unexpected revenue losses during the year; Capital Reserves, which provide for normal replacement of existing capital plan and the financing of capital improvements; OPEB Reserves provide for funding of other post employment benefit liability; Cash Flow Reserves, which provide sufficient cash flow for daily financial needs; and Contingency Reserves provide for unanticipated expenditures.

The Town shall maintain the following general, special and strategic reserve funds:

- **Operating Reserves**—The maintenance of adequate operating reserves is essential to the financial strength and flexibility of the Town as a whole. Adequate operating reserves are integral parts of the financial structure of the Town and help make it possible for the Town to issue debt, among many other functions.
  - 1. **Undesignated Fund Balance**- Operating fund balance shall be maintained at sufficient levels to absorb unpredictable revenue shortfalls and to insure desired cash flow levels. With regard to the General fund, cash balances available at year end shall, in combination with the new revenues be sufficient to preclude any requirement for short-term debt to sustain Town operations. Should this fund balance fall below 5% of the "Fund Balance Floor," defined as General Fund revenue less state aid and appropriations to reserve accounts, a plan for expenditure reductions and/or revenue increases shall be submitted to the Board of Selectmen during the next budget cycle.
  - 2. **Free Cash** – This reserve provides for the temporary financing of unforeseen opportunities or needs of an emergency nature including increases in service delivery cost. This is the portion of undesignated fund balance certified by the Department of Revenue, Division of Local Services, as "Free Cash". Monies held in this reserve may be appropriated during the current budget year and may also

be used as a source of revenue for the ensuing budget year. Of all general fund reserves this is the most flexible.

- **Stabilization Fund** – a Stabilization Fund shall be maintained, under the provisions of MGL Chapter 40, Section 5B.
  1. The target funding level (TFL) for the Fund shall be an amount equivalent to 5% of the Town's prior year's Total General Fund Revenue less appropriations to reserve accounts. A Stabilization Fund Floor shall be established at 1.5% of the Town's prior year's Total General Fund Revenue less appropriations to reserve accounts. The Fund shall be funded only with Free Cash or one-time revenues.
  2. The Stabilization Fund may only be used under the following circumstances:
    - a. To support the operating budget when General Fund Net Revenue, as defined as Total Revenue less debt exclusions and state school building reimbursements, increases less than 2.5% from the prior fiscal year.
    - b. To fund capital projects, on a pay-as-you-go basis, when available Free Cash drops below \$2 million in any year and only if the Capital Stabilization Fund has reached its floor as defined in the Capital Stabilization Fund section of this policy.
  3. The level of use of the Stabilization Fund shall be limited to the following:
    - a. When supporting the operating budget under "2a" above, the amount drawn down from the fund shall be equal to the amount necessary to bring the year-over-year increase in the Town's prior year Net Revenue to 2.5%, or \$1 million, whichever is less. The draw down shall not occur in more than three consecutive fiscal years and the maximum shall not exceed \$2.5 million for the three year period.
    - b. When funding capital projects, on a pay-as-you-go basis under "2b" above, no more than \$1 million may be drawn down from the fund in any fiscal year. The draw down shall not occur in more than three consecutive fiscal years and the maximum shall not exceed \$2.5 million for the three year period.
  4. In order to replenish the Stabilization Fund if used, in the year immediately following any draw down, the Town shall formulate a plan to restore the Fund to the previously identified TFL. Said funding shall come from Free Cash.
- **Capital Stabilization Fund** a Stabilization Fund shall be maintained, under the provisions of MGL Chapter 40, Section 5B.
  1. The TFL for the Fund shall be an amount equivalent to 1% of the Town's prior year Total General Fund Revenues. A Capital Stabilization Fund Floor shall be established at \$25,000. The Fund shall be funded only with Free Cash or one-time revenues.
  2. The Capital Stabilization Fund may only be used under the following circumstances:
    - a. To fund projects which have been approved as part of the Town's Capital

Improvement Plan (CIP).

- **Other Post-Retirement Benefits (OPEB)** – a Stabilization Fund established per the provisions of MGL Chapter 40, Section 5B, and a Trust Fund established per the provisions of MGL Chapter 32B, Section 20 shall be utilized to reserve funds to offset the Town's OPEB liability.
  1. The aggregate target funding level (TFL) for these Funds shall be an amount equivalent to 5% of the OPEB unfunded actuarial liability.
    - a. An amount equal to no less than 1% of the OPEB unfunded actuarial liability shall be transferred to the Stabilization Fund from the Town's Health Insurance Trust Fund at the time that the Stabilization Fund is established. Annually, an amount equal to a minimum of 2.5% of the aggregate Fund balance of these Funds shall be appropriated to either Fund from the operating budget or Free Cash or both.
    - b. From time to time the Town shall analyze the balance in the Health Insurance Trust Fund to determine if additional funds can be transferred into the OPEB Funds.
  2. In order to replenish the Funds if used, in the year immediately following any draw down, the Town shall formulate a plan to restore the Funds to the previously identified TFL. Said funding shall come from Free Cash.
- **Overlay Reserve** – established per the requirements of MGL Chapter 59, Section 25, the Overlay is used as a reserve, under the direction of the Board of Assessors, to fund property tax exemptions and abatements resulting from adjustments in valuation. The Board of Selectmen shall, at the conclusion of each fiscal year, require the Board of Assessors to submit an update of the Overlay reserve for each fiscal year, including, but not limited to, the current balances, amounts of potential abatements, and any transfers between accounts. If the balance of any fiscal year overlay exceeds the amount of potential abatements, the Board of Selectmen may request the Board of Assessors to declare those balances surplus, for use in the Town's Capital Improvement Plan (CIP) or for any other one-time expense.
- **Enterprise Fund Retained Earnings Reserve** – to provide rate stability in the Water and Sewer Enterprise Funds, the funds will maintain retained earnings equivalent to a minimum of three months of appropriated expenses. Retained earnings in excess of four months will be appropriated to offset user fees directly or indirectly through capital project pay-as-you-go funding of enterprise fund projects.
- **Special Education Stabilization Fund** – to provide stability in the delivery of public education that could otherwise be adversely impacted by costs associated with special education which were unforeseen at the time the annual fiscal appropriation was adopted by an Annual Town Meeting, the Town will establish a Stabilization Fund per the provisions of MGL Chapter 40, Section 5B. For the purpose of this policy unforeseen costs are those for which neither experience or reasonable judgment or planning could

have anticipated.

1. The target funding ceiling (TFC) for this Fund shall be \$750,000 and the target funding floor (TFF) shall be \$100,000.
2. The school department can request a transfer from this Fund in an amount not to exceed \$250,000 in any one fiscal year if the following conditions are met:
  - a. Eligible costs are limited to out of district placements and transportation costs associated with out of district placements.
  - b. The costs were unforeseen prior to the adoption by Town Meeting of the school department budget in the fiscal year the funds are being requested.
  - c. The School Committee, Finance Committee, and Board of Selectmen each by majority vote affirm that the costs were unforeseen and paying said costs from the appropriated school department budget would adversely impact the delivery of education in North Andover.
3. In order to ensure that the Fund is not depleted, and that proper financial planning is undertaken to reduce the likelihood of future unforeseen costs, the aggregate amount of transfers from the Fund in any two consecutive fiscal years is \$400,000. The Town shall formulate a plan to restore the Fund to the identified TFC when the balance of the Fund drops below the TFF. Said funding shall come from Free Cash or other Reserves.

Note: Transfers from this Fund will require action at a Special Town Meeting.